Corporate America
Credit Union

December 18, 2009

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Ms. Rupp:

We would like to express our appreciation to the NCUA Board for allowing us to comment on the proposed corporate credit union regulation.

704.3(c) Perpetual Contributed Capital

The proposed regulation eliminates the prohibition of conditioning membership and, therefore, services on a credit union's purchase of permanent capital. This can result in a natural-person credit union being forced to invest at risk capital deposits into a corporate credit union that may not be displaying the best stewardship of its members' funds. In December 2008, the NCUA Board granted U.S. Central a waiver of the applicable regulation. U.S. Central immediately conditioned membership (and therefore access to payment systems) on the purchase of permanent capital. The result was that the members of U.S. Central were effectively held hostage by the failing wholesale corporate.

The prohibition against conditioning membership/services on the purchase of permanent capital should remain in the regulation. At a minimum, a member credit union should be provided a twelve-month window to exercise an orderly termination of its services with the requiring corporate. This is necessary to ensure that the credit union's members are not immediately placed in a position whereby their access to payment systems is eliminated.

704.3(c)(3) Perpetual Contributed Capital Call Feature

This section precludes a corporate from exercising the call feature for perpetual capital without prior approval from NCUA. The decision regarding the exercise of this feature should remain with the issuing corporate. The NCUSIF remains protected by virtue of

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the capital requirements outlined in the proposed regulation. NCUA is overreaching in requiring preapproval.

704.3(d)(4)(v) Increased Individual Capital Requirement

This section vests an inordinate amount of power in the Director of the Office of Corporate Credit Unions (OCCU). Specifically, the final sentence states that "this decision represents final agency action." In essence, the Director of the OCCU can arbitrarily increase the capital required for a single corporate, and there exists no appeals process.

704.3(e)(3) Disallowing Capital from Inclusion in Ratios

This section also places an inordinate amount of authority in the Director of the OCCU since he can unilaterally require that certain capital accounts be discounted and not be included in the applicable capital ratios. If a capital account meets the definitions contained in the regulation, no NCUA employee should be granted the power to unilaterally decide that the capital account will not be included in the governing capital ratios.

704.4(d)(3) Lowering the Capital Category

Once again, the power vested in the Director of the OCCU leads to the potential for abuse. In this case the proposed regulation states that the Director of the OCCU can unilaterally change the capital category of a corporate credit union. This could result in an adequately capitalized corporate being forced to comply with onerous restrictions based simply on the opinion of one NCUA employee. **This authority is extremely dangerous.**

704.4(d)(3)(ii) Lowering the Capital Category based on Ratings

The proposed regulation states that the NCUA may lower a corporate's capital in the event any CRIS category is rated a three or worse. I read this to mean any composite rating or any rating of the components. Given that there are twelve separate components, it is likely that at least one will be rated a three or worse. I request that the NCUA Board review the ratings for all corporates during the past five years and determine the percentage that had all of the components rated better than a three. I suspect the percentage will be near zero. Therefore, the Director of the OCCU would be able to lower the capital category of any corporate at any time.

704.4(d)(4) Lowering the Capital Category for Good Cause

This section simply transfers power from the NCUA Board to the Director of the OCCU. With this degree of power concentrated in one individual, the respective boards of all corporates will effectively be employees of the Director of the OCCU.

704.4(e)(5) Submission of a Capital Plan

The proposed regulation states that "an undercapitalized corporate credit union is subject to the provisions applicable to significantly undercapitalized credit unions until it has submitted, and NCUA has approved, a capital restoration plan." Why? Essentially, the OCCU can subject a corporate credit union to the restrictions reserved for significantly undercapitalized corporates for an undue length of time. This section appears gratuitous.

704.4(k)(1) Payment of Dividends

The proposed regulation precludes a corporate deemed undercapitalized from paying dividends on capital accounts. This prohibition should be applicable only to those corporate credit unions that are significantly or critically undercapitalized.

704.4(k)(2)(v) Powers over Undercapitalized Corporates

If a corporate is deemed undercapitalized (even if the Director of OCCU lowers the category from adequately capitalized), the NCUA will have the power to do any of the following:

- Eliminate or reduce dividends on any or all accounts;
- Force a merger;
- Restrict growth;
- Dissolve CUSOs;
- Remove the board;
- Fire management;
- Conserve the corporate; or
- Take any other action (vague)

These powers are authorized by reference to 704.4(k)(3)(ii). That section standing alone is only applicable to significantly or critically undercapitalized corporates. Unfortunately, section 704.4(k)(2)(v) allows the Director of the OCCU to apply them to those corporates that are merely undercapitalized.

Therefore, by exercising his power to lower individual capital categories, the Director of the OCCU can fire any employee and/or remove any board at any existing corporate. And he will be able to do so at any time he chooses for years to come.

I question the constitutionality of that broad power.

704.4(k)(6)(ii)(C) Charter or Bylaws for State Chartered Corporates

This section usurps the power of state regulators by allowing NCUA to preclude a bylaw change for state chartered corporates.

704.8(e) Average life mismatch modeling

The preamble to the regulation states that the average life mismatch tests are designed to enhance the measurement of risks associated with credit spread widening. While recent history has painfully demonstrated that certain securities were vulnerable to such credit spread widening, other securities were not. Specifically, government-backed securities actually increased in value as funds moved from risky assets into safer assets via a flight to quality.

As written, the proposed regulation will undoubtedly force corporate credit unions to invest in short-term securities that contain credit risk and reduce their respective positions in government-backed bonds with moderate WALs.

The solution would seem to be to require the average life mismatch modeling only on the book of business that contains securities with credit risk. In other words, securities that have a risk weighting of 20 percent or less should be excluded from the average life mismatch tests. To do otherwise is simply creating a situation where credit risk will increase and the effects of credit spread widening will be exacerbated.

704.8(h) Two-year average life

Many securities that are appropriate for a corporate credit union to own have a weighted average life in excess of two years. Specifically, SBA securities and FFELP student loan securities are highly liquid and generally have no caps. However, they typically have WALs in excess of two-years. These two products are among the best stores of excess liquidity in that they present no credit risk, have low liquidity risk, and have virtually no interest rate risk. By assigning an arbitrary limit on the maximum WAL of the investment portfolio, the proposed regulation will actually increase credit risk and liquidity risk on the balance sheet as opposed to reducing them.

704.8(k) Deposit Concentrations

The stated objective for limiting deposits from any one source to no more than ten percent of a corporate's assets is to reduce risks that arise from placing undue reliance on a single entity.

However, by limiting funds from any one source to no greater than ten percent of a corporate's assets, the proposed regulation would:

-force funds out of the credit union system;
-penalize corporates that acted responsibly with their members money; and
-deny natural-person credit unions their ability to invest in institutions they deem appropriate

While many natural-person credit unions would have benefited if this restriction was in place before the financial crises began, many more would have suffered. By limiting the amount of funds a credit union may place in a single corporate, the proposed regulation could have forced those credit unions to invest funds in different corporates. In that case, the management of the natural-person credit unions would have had unnecessary exposure to the investment practices of many institutions. This would have increased the risk of loss to those natural person credit unions since they would have been required to evaluate the balance sheets of multiple corporates instead of a single corporate.

If this limit is imposed, the likely scenario going forward is that the natural-person credit unions will withdraw funds from the system. This not only decreases the liquidity in the network (possibly leading to the forced sale of distressed securities currently held by U.S. Central and other corporates), the overall decreased liquidity in the system may result in the restriction of credit some natural-person credit unions would otherwise provide to their own members.

Of the corporates that caused their members no losses throughout this crises, some of them attain a significant portion of their deposits from large, natural-person credit unions. By forcing those solvent corporates to refund a large amount of their deposits back to the investing natural-person credit union members, the proposed ten percent limitation is penalizing the solvent corporates and their members.

A natural-person credit union can choose to invest an unlimited amount of funds in a bank if they conduct proper due diligence. Why, then, should they be precluded from investing the same funds in another credit union (corporate or otherwise) if they conduct the same due diligence? There are many natural-person credit unions that are extremely glad that their money was invested in certain corporates. If the proposed ten percent limit had been in place prior to this crisis, those credit unions could have lost money unnecessarily by virtue of them being forced to make deposits into other institutions. A credit union should have the right to choose into which financial institutions it places its money...and its trust.

An adequate solution to achieve the stated objective of NCUA can be met without this line-in-the-sand ten percent limit. I recommend that deposits from one source be limited to the greater of ten percent of a corporate's assets OR one hundred percent of a corporate's assets that carry a risk weighting of 20 percent or less. This will ensure that deposit concentrations are invested only in high quality, very liquid assets.

707.4 Prompt Corrective Action

In the interest of transparency, corporate credit unions should be required to disclose their capital category. By prohibiting the dissemination of that information, the proposed regulation hides important information as to the strength of individual corporates from their respective member/owners.

704.11(e) CUSOs

Data processing services are not included as a permissible activity for corporate credit unions. However, eight corporates own a CUSO (CNP, LLC) that performs data processing for corporate credit unions. The regulation should allow corporate CUSOs to perform data processing services or, at a minimum, pre-approve that activity per section 704.11(e)(3).

Appellate Process

I recognize that the exercise of many of the new powers I have addressed have a built-in appeals process. However, based on my experience as an NCUA employee and based on my recent dealings with the appeals process itself, I remain skeptical that the powers granted to the NCUA staff by this proposed regulation will held in check by the appellate provisions.

Conclusion

As written, the proposed regulation would:

- Vest the Director of the OCCU with an inordinate amount of power;
- Effectuate a "power-grab" by the federal government;
- Render the elected boards of all corporates ineffective and treat them as subservient to NCUA employees;
- Cast aside the powers now reserved for state regulatory agencies;
- Reduce liquidity in the credit union system; and
- Increase credit risk

Please don't let this happen. Natural-person credit unions did not cause the problems being experienced by some of the corporates. Don't take away their ability to manage their own corporate credit unions.

Again, thank you for providing us with the opportunity to respond to the proposed regulation.

Sincerely,

Thomas D. Bonds, CPA
Attorney at Law
President & CEO